

## How TARP and QE Led to the “Green New Deal”

**Brian S. Wesbury** – Chief Economist  
**Robert Stein, CFA** – Dep. Chief Economist  
**Strider Elass** – Senior Economist

The most important quote from the Financial Panic of 2008 came from President Bush: “I’ve abandoned free market principles to save the free market system.”

The quote came in defense of TARP, the \$700 billion bailout of the banking system, which many still mistakenly believe prevented another Great Depression. Many also think Quantitative Easing, the Fed’s multi-trillion dollar purchases of Treasury and mortgage-backed securities, was also key in “saving” us from the free market. But the facts dispute this. QE began in September 2008, TARP was passed in early October, but the market fell an additional 40%. It didn’t bottom until it was clear that mark-to-market accounting rules would be changed.

The Bush Treasury, the Fed, and the SEC were all aware of the problems mark-to-market was causing. The accounting rule forced banks to value securities at fire sale prices regardless of their actual cash flow. This eroded bank capital which scared away investors and caused an even greater impulse to sell. Many prominent bankers, economists, and politicians were very vocal about the damage the rule was causing. But the Administration rallied support from journalists and hedge funds (who profited from the carnage mark-to-market accounting caused) to support a massive growth in government. It was the wrong choice.

In the 1980s, losses at money-center banks due to defaults by emerging market countries, losses at Savings & Loans, and farm and oil bank failures were much larger relative to bank capital than subprime losses in 2008-09. But there was no mark-to-market accounting back then. The Reagan Administration gave these institutions the ability to grow themselves out of the problem, which many did during the economic boom of the 1980s. After giving them time, the banks and S&Ls that couldn’t grow out of their problems were shut down. The banking system survived without a crisis. If the Bush Administration had followed Reagan’s lead, the crisis would never have spiraled.

But that’s not the worst part. Republicans are supposed to support free markets because free markets actually work. This matters most in the middle of a storm – either you believe in

your basic philosophy or you don’t. In this case not only did Republicans violate free market principles, but argued the government had to save the world, and bailed out big banks and Wall Street – the rich guys! What a political disaster.

When believers in free markets support bailouts, any objection to using the government to redistribute funds to others is just snobbery or hypocrisy. And, in turn, why not use the government to fix what are perceived by many to be major collective problems, like health care, or climate change or poverty.

Which brings us the “Green New Deal,” the mother of all big-spending social programs and government micro-management rolled into one, including a massive shift in energy toward 100% renewables (think, solar and wind power, not nuclear) in about ten years, a shift from air travel to rail, retrofitting every building in the US to save energy, the replacement of traditional car engines for electric cars, a much higher minimum wage, “Medicare for All,” and a bevy of other ideas. Mundane behavior like eating meat could also be in the crosshairs due to “emissions” from cows.

One estimate by a Bloomberg columnist suggests these proposals could carry a total cost of \$6.6 trillion per year. To put that in perspective, in the past twelve months the federal government has raised \$3.3 trillion in revenue, including \$1.7 trillion in individual income taxes, and spent \$4.2 trillion. In other words, it’s an impossible fantasy that would require tax collections at least three times higher than today. To think this wouldn’t reduce the incentive to work, while increasing the incentive to not work is denial.

On top of current taxes – federal, state, and local – plus the cost of regulations, the government would control around 70% of GDP. Which is to say that the proposal will not become law, or even close.

However, we hope this serves as a lesson to policymakers who proclaim their support for free markets. A decade ago, too many of these “principled” politicians turned out to be “fair weather” free-marketeers. When the going got rough, they gave up. And they are, in large part, to blame for more radical proposals today.

| Date/Time (CST) | U.S. Economic Data             | Consensus | First Trust      | Actual | Previous  |
|-----------------|--------------------------------|-----------|------------------|--------|-----------|
| 2-21 / 7:30 am  | Initial Claims – Feb 16        | 228K      | <b>232K</b>      |        | 239K      |
| 7:30 am         | Durable Goods – Dec            | +1.7%     | <b>+3.0%</b>     |        | +0.7%     |
| 7:30 am         | Durable Goods (Ex-Trans) – Dec | +0.3%     | <b>+0.7%</b>     |        | -0.4%     |
| 7:30 am         | Philly Fed Survey – Feb        | 14.0      | <b>19.9</b>      |        | 17.0      |
| 9:00 am         | Existing Home Sales – Jan      | 5.000 Mil | <b>4.980 Mil</b> |        | 4.990 Mil |